

Message Text

SECRET

PAGE 01 LONDON 12238 01 OF 03 020839Z
ACTION EB-04

INFO OCT-01 SS-04 ISO-00 EUR-03 NSC-04 CEA-01 FRB-03
INR-01 CIAE-00 SSO-00 INRE-00 /021 W
-----043195 020903Z /20
O 020824Z AUG 78
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 8709
TREASURY DEPT WASHDC IMMEDIATE

S E C R E T SECTION 01 OF 03 LONDON 12238

LIMDIS GREENBACK

TREASURY PASS ASSISTANT SECRETARY LUBICK, DEPUTY
ASSISTANT SECRETARY WIDMAN AND DONALD SYVRUD

E.O. 11652: XGDS-1
TAGS: EFIN, UK
SUBJECT: PROPOSED CHANGES IN NORTH SEA FISCAL REGIME

REF: LONDON 11706

SUMMARY: SENIOR SOURCES AT HM TREASURY AND INLAND
REVENUE REPORT THAT IN ALL LIKELIHOOD JOEL BARNETT, MP,
CHIEF SECRETARY IN HMT, WILL MAKE A STATEMENT IN
PARLIAMENT THIS AFTERNOON ANNOUNCING INTENTION TO RAISE
THE LEVEL OF PETROLEUM REVENUE TAX (PRT) FROM 45 PERCENT
TO 60 PERCENT FOR CHARGEABLE PERIODS AFTER DECEMBER 31,
1978; REDUCING THE UP-LIFT ON CAPITAL EXPENDITURE
ALLOWED AGAINST PRT FROM 75 PERCENT TO 35 PERCENT ON
CONTRACTS ENTERED INTO AFTER TODAY AND REDUCING THE OIL
ALLOWANCE WHICH IS EXEMPT FROM PRT FROM ONE MILLION LONG
TONS A YEAR SUBJECT TO AN OVERRIDING MAXIMUM OF TEN
MILLION TONS TO A LOWER FIGURE OF 500 THOUSAND METRIC
TONS A YEAR FROM JANUARY 1, 1979 WITH A MAXIMUM OF 5
MILLION TONS. THE CABINET WILL MEET THIS MORNING TO
SECRET

SECRET

PAGE 02 LONDON 12238 01 OF 03 020839Z

CONFIRM ABOVE AND ALSO TO DECIDE WHETHER BRITISH NATIONAL
OIL CORPORATION OPERATIONS ARE TO BE MADE SUBJECT TO PRT;
THIS APPARENTLY REMAINS AN UNSETTLED AND CONTENTIOUS
ISSUE. THE ABOVE INFORMATION UNTIL PUBLICLY ANNOUNCED
IS CONSIDERED BY HMG TO BE SECRET; IS BEING PROVIDED TO
USG ON THAT BASIS FOR VERY LIMITED DISTRIBUTION ONLY;
ANY PREMATURE DISCLOSURE BY THE USG OF THE INFORMATION

BEFORE IT IS ANNOUNCED TO PARLIAMENT WOULD BE VIEWED
AS A BREACH OF CONFIDENCE OF UTMOST GRAVITY. END SUMMARY

1. ON TUESDAY, AUGUST 1, "AS A MATTER OF COURTESY TO
U.S. TREASURY AND U.S. GOVERNMENT" TREASURY REP WAS
BRIEFED SEPARATELY BY SIR LAWRENCE AIREY, SECOND
PERMANENT SECRETARY, HM TREASURY AND BY SENIOR SOURCES
IN INLAND REVENUE ON STATEMENT THAT IS SCHEDULED TO BE
MADE IN PARLIAMENT AFTERNOON OF WEDNESDAY, AUGUST 2,
BY JOEL BARNETT, MP, CHIEF SECRETARY. INLAND REVENUE
SPECIFICALLY ASKED THAT INFORMATION NOT BE SENT TO
WASHINGTON UNTIL THIS MORNING. SOURCES STRESSED
INFORMATION MUST BE CONSIDERED SECRET BETWEEN GOVERNMENTS
AND GIVEN ONLY VERY LIMITED DISTRIBUTION IN USG UNTIL
THERE IS AN ACTUAL STATEMENT TO THE PARLIAMENT. WHAT
FOLLOWS IS THE BEST ESTIMATE OF THE SENIOR HM TREASURY
AND INLAND REVENUE STAFF OF WHAT ACTUALLY WILL BE SAID,
BUT DETAILS REMAIN SUBJECT TO CHANGE AT A CABINET
MEETING SCHEDULED TO BE HELD LATER THIS MORNING
(AUGUST 2).

2. AIREY SAID THE DRAFT STATEMENT PREPARED FOR BARNETT
CURRENTLY READS AS FOLLOWS:

"IT IS NOW MORE THAN THREE YEARS SINCE THIS
GOVERNMENT INTRODUCED THE PETROLEUM REVENUE TAX ON
SECRET

SECRET

PAGE 03 LONDON 12238 01 OF 03 020839Z

PROFITS FROM THE PRODUCTION OF OIL WON UNDER UNITED
KINGDOM PRODUCTION LICENSES AND WE HAVE BEEN REVIEWING
THE FISCAL REGIME FOR THE NORTH SEA TO SEE WHETHER ANY
CHANGES ARE CALLED FOR IN THE LIGHT OF EXPERIENCE. WE
HAVE COME TO THE CONCLUSION THAT THERE IS SCOPE FOR
INCREASING THE SHARE OF NORTH SEA PROFITS WHICH THE
GOVERNMENT RECEIVES.

WHEN WE FIXED THE RATES AND ALLOWANCES FOR PRT
AT THE BEGINNING OF 1975 WE DELIBERATELY ADOPTED A
CAUTIOUS APPROACH. WE SET THE RATE OF PRT NO HIGHER
THAN 45 PER CENT, AND WE GAVE GENEROUS ALLOWANCES AND
RELIEFS. INDEED, WE WERE CRITICISED FOR EXCESSIVE
GENEROSITY TO THE OIL COMPANIES.

NOW, HOWEVER, THOUGH MANY UNCERTAINTIES REMAIN,
WE ARE IN A POSITION TO TAKE STOCK AND WHAT HAS BECOME
APPARENT IS THAT COMPANIES ARE STILL ABLE TO GET VERY
LARGE PROFITS FROM THE NORTH SEA. WE BELIEVE THAT THE
PUBLIC SHARE OF THESE PROFITS SHOULD BE INCREASED.

WE DO NOT PROPOSE TO ALTER THE STRUCTURE OF THE
TAX OR TO REMOVE THE FRONT-END LOADING OF ALLOWANCES.

SECRET

NNN

SECRET

PAGE 01 LONDON 12238 02 OF 03 020844Z
ACTION EB-04

INFO OCT-01 SS-04 ISO-00 NSC-04 CEA-01 FRB-03 INR-01
CIAE-00 SSO-00 INRE-00 /018 W
-----043260 020900Z /20

O 020824Z AUG 78
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 8710
TREASURY DEPT WASHDC IMMEDIATE

S E C R E T SECTION 02 OF 03 LONDON 12238

LIMDIS GREENBACK

BUT WE DO PROPOSE THAT THE RATE OF PRT SHOULD BE INCREASED FROM 45 PER CENT TO 60 PER CENT FOR CHARGEABLE PERIODS ENDING AFTER 31 DECEMBER 1978. WE PROPOSE ALSO THAT THE 75 PER CENT UPLIFT AGAINST PRT SHOULD BE REDUCED TO 35 PER CENT IN RESPECT OF QUALIFYING EXPENDITURE UNDER CONTRACTS ENTERED INTO AFTER TODAY. THERE WILL BE SPECIAL TRANSITIONAL ARRANGEMENTS FOR EXPENDITURE UNDER CONTRACTS ALREADY ENTERED INTO: THE DETAILS ARE SET OUT IN A PRESS STATEMENT ISSUED TODAY BY THE TREASURY. I AM MAKING COPIES AVAILABLE TO HON MEMBERS FROM THE VOTE OFFICE.

IN ADDITION, WE PROPOSE THAT THE OIL ALLOWANCE, AT PRESENT 1 MILLION LONG TONS A YEAR SUBJECT TO AN OVERRIDING MAXIMUM OF 10 MILLION TONS, SHOULD BE REDUCED FROM 1 JANUARY 1979 TO 1/2 MILLION METRIC TONNES A YEAR WITH A MAXIMUM OF 5 MILLION TONNES.

PROVISIONS TO GIVE EFFECT TO THESE PROPOSALS WILL BE INCLUDED IN NEXT YEAR'S FINANCE BILL. TAKING ACCOUNT OF CORPORATION TAX, AND WITH PRT CONTINUING TO BE DEDUCTIBLE FOR CORPORATION TAX, WE ESTIMATE THAT THESE PROPOSALS WILL INCREASE GOVERNMENT TAKE BY ABOUT POUNDS 150 MILLION IN THE FINANCIAL YEAR 1979/80. AS REGARDS LATER YEARS, ESTIMATES OF THIS NATURE EXTENDING
SECRET

SECRET

PAGE 02 LONDON 12238 02 OF 03 020844Z

OVER A LONG PERIOD ARE, OF COURSE, HIGHLY SENSITIVE TO THE ASSUMPTIONS MADE ABOUT THE LEVEL OF OIL PRICES, EXCHANGE RATES, COST ESCALATION AND THE FLOW OF RECEIPTS AND BECAUSE OF THE UNCERTAINTIES INVOLVED ESTIMATES CAN ONLY SAFELY BE REGARDED AS INDICATING APPROXIMATE ORDERS OF MAGNITUDE. AS THE YIELD FROM PRT BUILDS UP, WITH MORE FIELDS COMING ON STREAM, WE ESTIMATE THAT BY THE MIDDLE 1980'S GOVERNMENT TAKE WILL BE INCREASED BY SOMETHING OVER 2 BILLION POUNDS IN TOTAL AND BY ABOUT .4 BILLION POUNDS A YEAR THEREAFTER AT TODAY'S PRICES.

THE OIL ALLOWANCE AT ITS NEW LEVEL WILL CONTINUE TO BE OF PARTICULAR VALUE TO SMALL FIELDS. THE SAFEGUARD PROVISIONS - WHICH PROVIDE THAT NO PRT IS PAYABLE IF THE PROFIT BEFORE CORPORATION TAX IN ANY YEAR FALLS BELOW 30 PER CENT OF HISTORIC CAPITAL COST - WILL REMAIN UNCHANGED; BUT IF, NEVERTHELESS, THERE ARE ANY WORTHWHILE DEVELOPMENTS, INCLUDING THOSE UNDERTAKEN PART-WAY THROUGH A FIELD'S LIFE, WHICH PROVE TO BE UNECONOMIC UNDER THE PROPOSED NEW RATES, THE GOVERNMENT WILL STILL HAVE THE MEANS OF ASSISTING THEM IN THE SHAPE OF POWERS OF MY RT. HON FRIEND THE SECRETARY OF STATE FOR ENERGY IN CONJUNCTION WITH THE TREASURY TO REFUND ROYALTIES FREE OF PRT AND CORPORATION TAX. UP TO NOW WE HAVE NOT HAD TO USE THESE POWERS BUT MINISTERS STAND READY TO DO SO IN APPROPRIATE CIRCUMSTANCES IN ORDER THAT DEVELOPMENTS WHICH ARE IN THE NATIONAL INTEREST GO AHEAD. ANY COMPANY READY TO PROCEED WITH DEVELOPMENT PLANS WHICH SEEM UNLIKELY TO PROVE ECONOMIC WITHOUT A REFUND OF ROYALTY SHOULD CONTACT MY RT. HON FRIEND IF THEY WISH SUITABLE ARRANGEMENTS TO BE EXAMINED.

X X X X X X X X

AS I HAVE STATED THESE PROPOSALS WILL BE INTRODUCED IN NEXT YEAR'S FINANCE BILL. HOWEVER THIS EARLY ANNOUNCEMENT IS

SECRET

PAGE 03 LONDON 12238 02 OF 03 020844Z

MENT WILL GIVE AMPLE OPPORTUNITY FOR THE OIL COMPANIES TO CONSIDER THEM AND, IF THEY WISH, TO DISCUSS THEM WITH THE INLAND REVENUE.

MY RT HON FRIEND THE SECRETARY OF STATE FOR ENERGY IS NOW SEEKING APPLICATIONS FOR THE SIXTH ROUND OF OFFSHORE LICENSING. THE GOVERNMENT THOUGHT IT RIGHT TO ANNOUNCE THEIR INTENTION ON TAXATION AT THE SAME TIME.

THE GOVERNMENT ARE ANXIOUS TO CONTINUE TO DEVELOP THE NORTH SEA ON THE BASIS OF PARTNERSHIP BETWEEN THE PRIVATE SECTOR AND THE PUBLIC SECTOR. BUT A BALANCE MUST BE STRUCK BETWEEN THE NEED TO SECURE FOR THE COMMUNITY A FAIR SHARE OF THE BENEFITS ARISING FROM THE NATIONAL RESOURCE WHICH THE NORTH SEA REPRESENTS, AND THE NEED TO LEAVE THE PRIVATE SECTOR WITH A RATE OF RETURN

WHICH IS FAIR IN THE LIGHT OF THE RISKS INVOLVED. THE GOVERNMENT ARE SATISFIED THAT THE CHANGES WHICH I HAVE JUST ANNOUNCED WILL MORE NEARLY ACHIEVE THIS BALANCE."

3. THE SUBSTANCE OF THE ABOVE WAS CONFIRMED IN SEPARATE CONVERSATION WITH A SENIOR SOURCE AT INLAND REVENUE, WHO ASKED THAT TREASURY ASSISTANT SECRETARY LUBICK BRIEF SECRETARY BLUMENTHAL "TO THE EXTENT THAT HE CONSIDERS NECESSARY". INLAND REVENUE SOURCE, WHO SAW NO POINT IN BEING IDENTIFIED, SPECIFICALLY CONFIRMED THE INCREASE IN PRT RATE, THE DECREASE IN THE UPLIFT, THE CUT IN THE OIL ALLOWANCE AND CONFIRMED REVENUE ESTIMATES CITED IN ABOVE TEXT BUT DID NOT GO FURTHER THAN THIS, BEING MUCH MORE CAUTIOUS THAN HM TREASURY. AIREY

SECRET

NNN

SECRET

PAGE 01 LONDON 12238 03 OF 03 020847Z
ACTION EB-04

INFO OCT-01 SS-04 ISO-00 NSC-04 CEA-01 FRB-03 INR-01
CIAE-00 SSO-00 INRE-00 /018 W
-----043296 020859Z /20

O 020824Z AUG 78
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 8711
TREASURY DEPT WASHDC IMMEDIATE

S E C R E T SECTION 03 OF 03 LONDON 12238

LIMDIS GREENBACK

ON THE OTHER HAND CLIPPED OUT OF ABOVE STATEMENT SECTION IN THE TEXT INDICATED BY X'S SAYING ONE MATTER REMAINED FOR DECISION BY THE CABINET THIS MORNING. INLAND REVENUE SOURCE SAID THAT THE ONE TOPIC NOT YET DECIDED IS WHETHER OR NOT OPERATIONS OF THE BRITISH NATIONAL OIL CORPORATION WILL BE SUBJECT TO PRT.

4. AMONG THE QUESTIONS AND ANSWERS PREPARED FOR POSSIBLE USE BY HMG ARE TWO RELATING TO THE U.S.-U.K. DOUBLE TAX TREATY:

HOW DO THE PRESENT PROPOSALS AFFECT THE UK/US DOUBLE TAXATION TREATY? WILL NOT THE US RESTRICT THE

CREDITABILITY OF PRT?

I CANNOT COMMENT ON THIS WHILE DISCUSSIONS ABOUT THE TREATY ARE TAKING PLACE IN THE LIGHT OF THE US SENATE'S RECENT DECISION ABOUT RATIFICATION.

IS THIS THE UK'S RESPONSE TO THE US DELETION OF ARTICLE 9(4) FROM THE DOUBLE TAXATION TREATY?

NO.

5. THE ABOVE STATEMENT HAS BEEN APPROVED BY THE PRIME MINISTER. BECAUSE OF ITS GENERAL IMPACT ON ENERGY POLICY, IT HAS BEEN THE SUBJECT OF GENERAL CABINET SECRET

SECRET

PAGE 02 LONDON 12238 03 OF 03 020847Z

DISCUSSION AND DECISION RATHER THAN MORE LIMITED DECISION BY THE CHANCELLOR, TREASURY AND INLAND REVENUE. AS NOTED, A CABINET MEETING THIS MORNING IS EXPECTED TO GIVE FINAL APPROVAL PRIOR TO AN ANNOUNCEMENT EXPECTED THIS AFTERNOON (ALTHOUGH BOTH SOURCES STRESSED USG MUST KEEP THE INFORMATION SECRET UNTIL THERE IS A FORMAL PUBLIC ANNOUNCEMENT AND IN ANY PUBLIC COMMENTS SHOULD BE GUIDED BY THE TEXT OF FORMAL ANNOUNCEMENT TO PARLIAMENT, WHICH COULD VARY FROM THE ABOVE DRAFT).

6. DURING DISCUSSIONS, SOURCES STRESSED THAT NOTHING BEING PROPOSED IS RETROACTIVE. POSSIBLE INCREASE IN PRT LEVEL HAS BEEN UNDER INCREASING REVIEW. IT WAS LOGICAL TO MAKE WHATEVER FISCAL CHANGES WERE CONSIDERED APPROPRIATE IN CONNECTION WITH THE SIXTH ROUND LICENSING PROVISIONS. SOURCES CONSIDERED INCREASE IN PRT "IS NOT REALLY MASSIVE", THE RETURNS ON LARGE FIELDS WILL BE REDUCED BY A FEW POINTS, SMALLER FIELDS WILL BE HIT HARDER, AND IT IS IN THIS AREA THAT THE GOVERNMENT WOULD EXPECT THE SECRETARY OF STATE FOR ENERGY IN CONJUNCTION WITH HM TREASURY TO REFUND ROYALTIES FREE OF PRT AND CORPORATE TAX IF FAILURE TO DO SO WOULD RESULT IN FIELDS NOT BEING DEVELOPED. HMG BELIEVES THAT MOST FIELDS WILL STILL MAKE HANDSOME PROFITS AND THE LARGEST SUFFERER IN TERMS OF A SPECIFIC COMPANY WILL BE BRITISH PETROLEUM.

7. SOURCES DID NOT BELIEVE THAT THE ABOVE MEASURES WOULD BE TOO CONTENTIOUS. COMPANIES WILL OF COURSE OBJECT BUT SOURCES DOUBT THAT THEY WOULD ACTUALLY BE SCARED OFF FROM FURTHER NORTH SEA ACTIVITY. THE ROLE OF THE BRITISH NATIONAL OIL CORPORATION IN THE SIXTH LICENSING ROUND IS SEEN AS MUCH MORE CONTROVERSIAL.

SECRET

SECRET

PAGE 03 LONDON 12238 03 OF 03 020847Z

8. DISCUSSING IMPACT ON THE U.S., INLAND REVENUE SOURCE CONSIDERED THAT BECAUSE OF THE KENNEDY AMENDMENT, LIMITING PRT TO A COUNTRY BASIS, OIL COMPANIES WILL BE IN AN EXCESS CREDIT POSITION AND THERE WILL BE LITTLE IF ANY TAX LOSS TO THE US TREASURY AS A RESULT OF THE ABOVE CHANGES. WHERE THE IMPACT WILL BE FELT IS OVER THE FOREIGN EXCHANGE, BECAUSE THERE ARE BALANCE OF PAYMENT IMPLICATIONS. THERE WOULD BE AN IMMEDIATE REDUCTION IN OUTFLOWS FROM THE U.K. OF NET OF TAX INTEREST, PROFIT AND DIVIDENDS FROM OVERSEAS INVESTMENTS IN THE NORTH SEA. THE LONGER TERM IMPACT WILL DEPEND ON HOW INVESTMENT FLOWS ASSOCIATED WITH THE NORTH SEA PROGRAM ARE AFFECTED.

9. THE ABOVE PROPOSED CHANGES ARE SUBJECT TO PARLIAMENTARY APPROVAL IN THE NEXT LEGISLATIVE SESSION. IT IS FAIRLY PROBABLE THAT AN ELECTION WILL INTERVENE BETWEEN NOW AND THEN. ON THIS ASSUMPTION, IT IS UNLIKELY THAT OIL COMPANIES WILL ACTUALLY ENTER THEIR SIXTH ROUND LICENSING BIDS UNTIL RESULTS OF THE ELECTION ARE KNOWN. SOME SENIOR TECHNICIANS IN HMG DO NOT BELIEVE THE CONSERVATIVE PARTY, IF IT WERE TO WIN THE NEXT ELECTION, WOULD MAKE ANY MAJOR CHANGES IN THE SUBSTANCE OF THE ABOVE PROPOSALS.

10. EMBASSY WILL CABLE ACTUAL TEXT OF UNCLASSIFIED STATEMENT TO PARLIAMENT ASAP.
BREWSTER

SECRET

NNN

Message Attributes

Automatic Decaptioning: Z
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: PETROLEUM PRODUCTION, TAXES
Control Number: n/a
Copy: SINGLE
Draft Date: 02 aug 1978
Decaption Date: 20 Mar 2014
Decaption Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 20 Mar 2014
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978LONDON12238
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: X1
Errors: N/A
Expiration:
Film Number: D780315-1193
Format: TEL
From: LONDON
Handling Restrictions:
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t197808108/aaaadmkk.tel
Line Count: 362
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 5c0c8b58-c288-dd11-92da-001cc4696bcc
Office: ACTION EB
Original Classification: SECRET
Original Handling Restrictions: LIMDIS
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 7
Previous Channel Indicators: n/a
Previous Classification: SECRET
Previous Handling Restrictions: LIMDIS
Reference: 78 LONDON 11706
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 30 jun 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 1563147
Secure: OPEN
Status: NATIVE
Subject: PROPOSED CHANGES IN NORTH SEA FISCAL REGIME
TAGS: EFIN, UK
To: STATE TRSY
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/5c0c8b58-c288-dd11-92da-001cc4696bcc
Review Markings:
Sheryl P. Walter
Declassified/Released
US Department of State
EO Systematic Review
20 Mar 2014
Markings: Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014